

TRADE AND AMERICAN ECONOMIC STRATEGY: THE CASE OF CHINA'S WTO ACCESSION

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Philadelphia, PA

April 6, 2000

Thank you very much. I am pleased to be here with you, and grateful to the Wharton School for this chance to speak on one of America's most important trade and foreign policy goals: China's accession to the World Trade Organization. and permanent Normal Trade Relations status.

ONE-WAY CONCESSIONS

In the most basic sense, of course, these are technical trade policy issues. And when we consider them as such, we have a clear economic choice:

Last November, after years of negotiation, we reached a bilateral agreement with China on WTO accession. It secures comprehensive, one-way concessions, opening China's markets to America's industrial goods, agriculture and services. It strengthens our guarantees of fair trade, and our ability to enforce Chinese commitments. By contrast, we change none of our market access policies; in a national security emergency, we can withdraw the market access China has now. We change none of our trade laws, and none of our laws controlling the export of sensitive technology. We agree only to maintain the market access policies we already apply to China, and have for over 20 years, by making China's current Normal Trade Relations status permanent.

Permanent NTR is the only issue before Congress. Regardless of the Congressional debate, China will enter the WTO. Regardless of the debate, it will retain its market access in America. The only question now is whether we will accept the benefits of the agreement we negotiated; or on the contrary, by turning away from permanent NTR, give these benefits to our trade competitors while American entrepreneurs, farmers and factory workers are left behind.

THE TRADING SYSTEM IN AMERICAN FOREIGN POLICY

From the strict perspective of American economic self-interest, this is fairly stark and simple. In this light we could end the discussion right there. But China's accession also has implications for many of the broader goals at the foundation of our modern trade policies. And these topics that I will concentrate today.

For over five decades, Americans have led in development of an open world economy

under the rule of law. We have done so for reasons reflecting, first of all, clear economic logic. Open markets abroad offer our businesses, farmers and workers larger markets: almost 80% of world economic consumption takes place outside the U.S., and to grow and remain competitive in the future, America must have fair access to these markets. At the same time, open markets at home give us access to imports, which dampen inflation; spark the competition that promotes innovation and efficiency; and raise living standards, most of all for the poorest among us.

These are ideas with broad application. We tend to believe they reflect Western liberal thought, but one can also cite the classical Chinese historian Ssu-ma Ch'ien, writing in 90 B.C.:

"There must be farmers to produce food, men to extract the wealth of mountains and marshes, artisans to process these things, and merchants to circulate them. There is no need to wait for government orders: each man will do his part as he gets what he desires. So cheap goods will go where they fetch more, while expensive goods will make men search for cheap ones. When all work willingly at their trades, just as water flows ceaselessly downhill day and night, things will appear unsought and people will produce them without being asked."

Today's World Trade Organization is an attempt to create such an economy for ourselves and our trading partners: to open markets, strengthen the rule of law, and by doing so raise living standards, promote technological progress and ultimately strengthen peace.

To trace it to its roots, the WTO reflects the lessons President Truman and his Allied counterparts drew from personal experience in Depression and war. In the 1930s, they had seen their predecessors fail to resist a cycle of protection and retaliation, including the Smoot-Hawley Act in the United States and colonial preference schemes in Europe, which had deepened the Depression and contributed to the political upheavals of the era. Eighteen years later, at the foundation of the WTO's predecessor, the General Agreement on Trade and Tariffs (GATT), they believed that by reopening world markets they could restore economic health and raise living standards. And as part of a broader array of policies and institutions -- economic stability through the IMF and World Bank; international standards of human rights, embodied in the Universal Declaration on Human Rights and a series of later Conventions; and the collective security commitments of the United Nations, NATO and our Pacific alliances -- they believed that open markets would give nations greater stakes in stability and prosperity beyond their borders, strengthening a fragile peace.

Since then, we have completed eight negotiating Rounds, and 112 new members have joined the 23 GATT founders. The agenda has broadened from tariffs -- which have dropped by 90% on average -- to non-tariff barriers, technical standards, dispute settlement, agriculture, services, intellectual property, telecommunications, information technology, financial services and electronic commerce. It continues today, with the WTO's decision in February to open negotiations on agriculture and services, and our work to broaden these talks into a new Round.

When we step back for a moment, we see the enormous benefits this has brought:

- Growth and Rising Living Standards: The opening of world markets has helped to spark what is in effect a fifty-year boom, in which trade has expanded fifteen-fold since the 1950s, world economic production grown six-fold and per capita income nearly tripled. And the result has been historically unprecedented social progress: since the 1950s, world life expectancy has grown by twenty years, infant mortality dropped by two-thirds, and famine receded from all but the most remote or misgoverned corners of the world. America, as the world's largest importer and exporter, benefits perhaps most of all.
- Economic Security: In the Asian financial crisis of 1997-99, with 40% of the world in recession, the respect WTO members had for their commitments kept open the markets necessary for affected nations to recover. Thus the system of mutual benefit and rule of law represented by the WTO helped prevent a cycle of protection and retaliation like that of the 1930s; and ultimately to avert the political strife that can erupt in economic crisis.
- Peace and Stability: Through the accession of 112 new members since 1948, the GATT and now WTO have helped us address some of the political challenges of greatest importance for world peace and stability. It helped to reintegrate Germany and Japan in the 1950s, and the nations emerging from colonial rule in the 1960s and 1970s. And it has now taken up a task of equal gravity, as after the Cold War, the nations breaking with communist planning systems – Albania, Croatia and Bulgaria; the Baltics, Ukraine, Russia, Georgia, and Armenia; the Kyrgyz Republic and Mongolia – seek WTO membership to reform their economies and integrate with the world.

CHINESE REFORM AND U.S. TRADE POLICY

And with this we come to China.

The world's largest nation, for many years, was one of the great rents in the trading system. When our modern relationship began in 1972, its economy was almost entirely divorced from the outside world. After the Communist revolution in 1949, it had expelled foreign businesses and banned direct economic contact between Chinese citizens and the outside world. At home it offered virtually no space for private farming or business; externally, it conducted what trade it felt necessary through a few Ministries. Such policies impoverished China and contributed to the revolutionary role China took up in Asia: isolated from Pacific markets, Asia's largest nation had little stake in a peaceful and stable region, and every Pacific nation felt the consequences.

In the intervening thirty years, American trade policy has worked to end this isolation. Our policies, viewed in detail, have sought concrete new opportunities for American businesses, workers, and farmers. But they also have pushed forward a strategic vision. By opening China's markets, and helping to give China access to world markets, we have sought to ensure that this

nation of 1.2 billion people plays its proper role as an export market and a source of economic growth for its Asian neighbors; promote reform and economic liberalization within China; and, ultimately, help China find a different and healthier role in the Pacific region.

This is a strategy consistent with China's own reforms. At home, since the 1970s, China has reversed the most damaging policies of the Great Leap Forward and Cultural Revolution era, abolishing rural communes and reviving private business in villages and cities. Domestically, reforms have established an internal market, eliminating many controls over prices; eroding the repressive "work-unit" system that bound workers to particular jobs and factories; reducing the state's role as an owner and manager of factories; and, over time, replacing bureaucratic control with law. Externally, reform has begun to open China to the world, substantially relaxing although not abandoning entirely bans on foreign investment and private export trade.

American trade policy has worked with reform at every step. This has been consistent and bipartisan, from the lifting of the trade embargo in 1972 under President Nixon, to our Bilateral Commercial Agreement and grant of Normal Trade Relations (then MFN status) in 1979 under President Carter; renewal of NTR every year since; our support for China's APEC membership; and in the 1990s detailed agreements on market access, intellectual property, textiles and agriculture. Each step rested on concrete American trade interests; each also helped advance reform in China, acquaint China with modern standards of business and governance, and integrate China into the Pacific and world economies.

To choose a case in point, our work on intellectual property rights since the early 1990s, based on our commitment to fight theft through piracy of our most creative industries, has helped us to nearly eliminate manufacturing and export of pirate CDs and CD-ROMs. But it means more than this: to develop an intellectual property policy is to draft and publish laws; to train lawyers and officials; to improve and ensure access to judicial procedures; ultimately, to create due process of law where it did not exist before. The same is true, more recently, with our work with the Chinese Ministry of Agriculture to develop modern sanitary and phytosanitary procedures.

This is one example of a much broader process of economic reform, opening to the world, and adoption of internationally accepted trade principles which have served China, its neighbors and ourselves well. At home, they have helped 200 million Chinese men and women escape from poverty. For us, they have sparked \$10 billion in export growth since our Commercial Agreement. And their advantages go beyond material gain.

While China remains an authoritarian and repressive country, reform has strengthened personal freedoms and begun to develop the rule of law. And it has made China a more integrated, responsible member of the Pacific community. To choose one example, when the Asian financial crisis began in 1997, South Korea and the ASEAN were (setting Hong Kong aside) the source of a seventh of China's foreign direct investment, and the market for a sixth of its exports. Thus, while in 1967 these nations were China's ideological rivals, today they are the customers who support Chinese factories and farm incomes, and the investors who create Chinese jobs. Thus China chose

in this event to maintain currency stability and contribute to recovery packages. The fact that the financial crisis did not become a security crisis owes much to this change in Chinese perceptions of its regional interests.

REFORM INCOMPLETE

But the work is not yet done. As the economist and reform advocate Cao Siyuan has put it, China has opened the door; but only to reach out and cautiously shake hands.

To look back again on the financial crisis, while China's policy was constructive, important and valuable, its neighbors did not have the opportunity to use China as a market which could spur recovery. ASEAN and Korean exports to China – already low – actually dropped by \$4.5 billion, or nearly 25%, between 1997 and 1998. Or to use another index, closer to home, our \$10 billion in export growth to China since 1980, while substantial, is far less than our export growth to almost any other major trading partner -- Europe, Japan, South Korea, ASEAN, Canada, Mexico, Taiwan or the Caribbean Basin countries -- over the same period.

This reflects the fact that reform remains incomplete. Some policy legacies of the revolutionary era remain in force today, and others are only partly reformed. Foreign companies may invest in China, but lose rights to import parts and market their products. China maintains a patchwork of geographical policies which encourage foreign investment in some areas while discouraging or banning it in others. State ownership of industry generally remains quite high. Beyond these unusual features of the Chinese economy are more typical trade barriers: China's high tariffs are joined by an array of largely secret quotas, and by industrial policies that require investors to transfer technology, purchase parts only from Chinese sources, and so forth. And more generally, the country still suffers from poorly developed market institutions and the lack of a reliable rule of law.

These are barriers to American products, but they are problems for China as well. Geographic limitations, for example, mean Chinese insurance regulators spend much of their time calculating whether a particular area might "need" one or two or three more companies rather than reviewing the financial health of insurance firms. Border barriers block agricultural and manufactured imports that could raise living standards and make Chinese business more productive. State monopolies in distribution mean that farmers lose much of their crop on the way to market. The financial sector is mired in debts, but is still making the majority of its loans to a loss-making state-owned enterprise sector that accounts for only around one-third of China's economic output. And overall economic inefficiency has made job creation difficult, leading to high unemployment rates just as immigration from rural districts to the cities accelerates.

Thus, just as China's external and internal trade barriers only block imports, they also – as China's senior leaders realize – have led to corruption and economic inefficiencies which block China's own prospects for sustainable growth, job creation and technological progress.

THE WTO ACCESSION

Against this background, the WTO accession assumes its full economic significance. The agreement we reached last November will address each barrier to American goods, services and agricultural products. It will take up all the major unfair trade practices we face in the Chinese market. And it will help China build an economy prosperous and open to the world, on the foundation of principles Ssu-ma Chi'en outlined 2100 years ago and the Wharton School teaches today. To offer you a look at the details:

- In manufacturing, China will cut industrial tariffs from an average of 24.6% in 1997 to 9.4% by 2005. China will eliminate all quotas and discriminatory taxes. And of critical importance, in virtually all products it will allow both foreign and Chinese businesses to market, distribute and service their products; and to import the parts and products they choose.
- In services, China's markets will open for the full range of sectors: distribution, telecommunications, financial services, insurance, professional, business and computer services, motion pictures, environmental services, law, architecture, construction, travel and tourism, and other industries. China will participate in the WTO's newest agreements on Financial Services and Basic Telecommunications. It will make historic commitments in the professions, from international law to accounting and management consulting. In some fields, such as distribution and telecom, this means the first opening to direct foreign participation since the 1940s.
- In agriculture, on U.S. priority products tariffs drop from an average of 31% to 14% by 2004. China will also expand access for bulk agricultural products; agree to end import bans, cap and reduce trade-distorting domestic supports; eliminate export subsidies and base food safety decisions on science.
- And American workers and businesses will receive stronger protection against unfair trade practices, import surges, and investment practices intended to draw jobs and technology to China. The agreement addresses state enterprise policies, forced technology transfer, local content, offsets and export performance requirements. It provides, for a 12-year period, a special remedy to discipline market-disrupting import surges from China. And it strengthens our antidumping laws by guaranteeing our right to use a special non-market economy methodology to address dumping for 15 years after China's accession to the WTO.

Each commitment is fully enforceable. China's commitments are specific and detailed; and as a fundamental WTO principle, China must for the first time publish all its laws and regulations. And WTO accession will not only ease enforcement but give us new tools: in addition to our trade laws, we will have WTO dispute settlement, periodic multilateral review of China's adherence, multilateral pressure from all 135 WTO members, and other mechanisms such as the special anti-dumping rules and anti-import surge remedies. We are preparing now, with the President's request for increased funding for China compliance and enforcement in his Fiscal Year 2001 budget.

CASE STUDY: THE AUTO INDUSTRY

To illustrate the cumulative effect of these commitments, let me offer a case study of the present situation and the changes WTO accession will make for the automobile industry.

At present, a combination of trade barriers and industrial policies makes it virtually impossible to export cars to China. Last year, the total was 419 cars, of which 130 were used. This figure is far less than a single average U.S. auto dealership sells in a year; it is actually fewer than the 688 motorized golf-carts we sold to China. To sell in China, therefore, an auto company must build its factories and hire its workers there; once it has done so, China requires transfer of technology, requires local purchases for parts, and restricts the right to market, finance and repair cars. Our bilateral agreement addresses each of these policies:

- We reduce barriers at the border, cutting auto tariffs from 80-100% today to 25% in 2006; forbidding discriminatory value-added taxes; and raising the current virtually prohibitive quota to \$6 billion worth of autos and then eliminating it entirely within five years.
- We open distribution markets and guarantee trading rights, ensuring that firms and dealerships in China can import autos directly from the United States, auto plants can buy American parts, and Americans can move their products freely within China to the areas of greatest demand.
- We open up services essential to auto sales: China will let auto firms provide financing, set up dealerships, advertise their cars, and provide repair and maintenance.
- We abolish certain industrial policies intended to draw auto investment, jobs and technology to China: China will abandon requirements that firms set up factories in China in order to sell in China, and abolish local purchase requirements and forced technology transfer as a condition of investment.
- We strengthen the security of auto production and jobs in the U.S. with the commitments on market-disrupting import surges and anti-dumping rules.
- And we have enforcement mechanisms for all these separate, overlapping commitments.

Thus, we in essence have a comprehensive agreement on automobile trade; and we match it, though specific features differ, in every industry of concern to the U.S. economy: from autos to information technology, wheat, finance, law, fishery products, pharmaceuticals, environmental technologies, steel, citrus, telecom and all the way down the list. Altogether, this will open China to American exports as never before; it will make China the source of growth and opportunity for the Pacific region that it should be; and it will place the capstone on thirty years of American support for reform, opening and change in China.

Finally, China's entry will facilitate Taiwan's entry into the WTO. This will have substantial trade benefits, as Taiwan is already a larger export market for us than China. And the opening of both economies, while we have no guarantees, may ultimately play some part in easing the tensions in the Strait. It should thus be no surprise that Taiwan's new leadership supports both China's WTO membership and normalized trade between China and the United States.

PERMANENT NORMAL TRADE RELATIONS

And this brings me to the point at which I began, with permanent NTR.

China will be a WTO member soon. There is no question of that. The only question, ironically, is whether we will receive the full benefits of the very agreement we negotiated.

By contrast to China's historic set of commitments, our sole obligation is to grant permanent NTR. In terms of our China policy, this is no real change. NTR is simply the tariff status we give to virtually all our trading partners. We have given it to China since the Carter Administration; every Administration and every Congress since has reviewed it and found it, even at the periods of greatest strain in our relationship, in our fundamental national interest.

But the legislative grant of permanent NTR is critical. All WTO members, including ourselves, pledge to give one another permanent NTR to enjoy the full benefits of one another's markets. Were Congress to refuse to grant permanent NTR, we thus risk losing broad market access, special import protections, and rights to enforce China's commitments through WTO dispute settlement. Our Asian, Latin American, Canadian and European competitors will reap these benefits; Americans would be left behind.

CONCLUSION

That in my view would be an extraordinary mistake. Such a U.S. retreat, at this most critical moment, would harm every significant interest we have in our relationship with China. And this is clear when we ask the most basic questions:

- Do we benefit from today's relatively open and inclusive world economy; or were Americans better off with the closed and exclusive world economy of the 1930s?
- Are we better off integrating China, Russia, Ukraine and the other reforming nations into the trading system we have built; or attempting to frustrate and isolate them?
- Should we support Chinese economic reform and opening to the world; or was our interest in a prosperous, stable Pacific better served by China's isolation in the 1950s and 1960s?
- Should the United States receive the benefits of China's entry to the WTO – or give them to everybody else?

Clearly, we are better off with today's open world economy than the closed world economy of the 1930s. We are better off integrating countries breaking with strict communist

planning than isolating them. We are better off with a reforming and opening China than an isolated and resentful China. And as China will enter the WTO regardless of our decision, we would simply be foolish to give the benefits of its accession to our competitors, while punishing our own farmers and factory workers.

In terms of our economic interests, therefore, to reject PNTR would be foolish; and as this brief set of questions implies, the damage would go well beyond economics and trade.

We have concerns and responsibilities towards human rights and the rule of law in China. In these areas, to reject permanent NTR is to turn our backs on nearly thirty years of work to support reform, improve the legal system and offer hope for a better life to hundreds of millions of Chinese. And it is to give up the hope of contributing in the future to a China freer, more open to the world, and more responsive to the rule of law than it is today.

And we have a fundamental national security interest in a peaceful, stable, mutually beneficial relationship with China. And in this sense, to reject PNTR would be reckless. No trade agreement will ever solve all our disagreements, but this will address many of them; and if we turn down a comprehensive set of one-way concessions, we make a very dark statement about the future possibility of a stable, mutually beneficial relationship with the world's largest country.

As the President has said, for every major American trade, economic and foreign policy interest, to reject PNTR would be to lessen the chance that China will choose the right path in the years ahead. And these are the stakes as Congress prepares to vote.

This is why the Administration is committed to permanent Normal Trade Relations status for China on the basis of this historic agreement.

And this is why it is so important that we succeed.

Thank you very much.